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FM AMEMBASSY HANOI

TO RUEHC/SECSTATE WASHDC IMMEDIATE 4624

INFO RUEHHM/AMCONSUL HO CHI MINH IMMEDIATE 2553

RUEATRS/DEPT OF TREASURY WASHINGTON DC IMMEDIATE

RUCPDOC/DEPT OF COMMERCE WASHINGTON DC IMMEDIATE

RHEHNSC/NATIONAL SECURITY COUNCIL WASHINGTON DC IMMEDIATE

RUEHGP/AMEMBASSY SINGAPORE IMMEDIATE 2279

RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION

UNCLAS SECTION 01 OF 03 HANOI 000290

SIPDIS

STATE FOR EB/OMA, EAP/MLS AND EAP/EP

TREASURY FOR ANDY BAUKOL, CAROL CARNES AND SUSAN CHUN

STATE PASS USTR DAVID BISBEE

SINGAPORE FOR SUSAN BAKER

SIPDIS

SENSITIVE

E.O. 12958: N/A

TAGS: [EFIN](#) [ECON](#) [ETRD](#) [EINV](#) [VM](#)

SUBJECT: TREASURY LETTER DELIVERED ON CAPITAL CONTROLS

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(U) This cable contains sensitive information and should not be placed on the internet.

REF: (A) HANOI 260

(B) HO CHI MINH 143

(C) Feb 13-14 e-mails from Treasury

¶1. (SBU) Summary. While no senior Vietnamese officials were willing to talk on the phone with Treasury about capital controls, a cooperative Office of Government official was amenable to receiving written comments. Embassy delivered a letter from Treasury DAS Dohner to Mr. Hung that discussed the importance of open capital markets for investment, the negative repercussions of controls, and alternative measures. On the private sector side, the Prime Minister has not responded to the Bank Working Group's February 7th request for a meeting. In the meantime, there was an unconfirmed market report this afternoon that a government committee met yesterday and voted against the proposed capital controls. End summary.

¶2. (SBU) Reflets reported Prime Minister Dzung is considering the imposition of capital controls in an effort to deal with an overheated stock market. On February 13, we tried to set up a phone call from Treasury Deputy Assistant Secretary for Asia Robert Dohner to a senior Vietnamese official in order to obtain more information about the rumored capital controls and to consult.

¶3. (SBU) First, we reached out to Finance Vice Minister Ha, but his office replied that the MOF is not responsible for the capital controls issue. They directed us to contact the State Bank of Vietnam (SBV). We did. Deputy Governor Nguyen Dong Tien replied that the capital controls issue is currently under consideration and decision of the Government, and thus beyond authority of the SBV and the Deputy Governor to speak or discuss the issue. Finally, we contacted Mr. Bui Huy Hung, International Relations Director in the Prime Minister's Office. Hung explained that capital controls are an extremely complex and sensitive issue and he preferred not to discuss it on the phone. He suggested, however, that Treasury provide written comments. (Comment: Hung has been a cooperative contact of the Embassy. He has been in the driver's seat on the Vietnamese side during the annual meetings under our Bilateral Trade Agreement (BTA). End comment.)

¶4. (SBU) We delivered the letter (ref C and full text in para 6) of Treasury Deputy Assistant Secretary Robert Dohner to Hung on

February 14. The letter expresses USG encouragement for open capital markets because of their importance in promoting foreign investment, describes the negative repercussions that capital controls can have on an economy, and suggests other policy alternatives that are available.

¶5. (SBU) Our contacts with Citibank indicate that the Prime Minister has not responded to the February 7th request of the Bank Working Group of the Vietnam Business Forum for a meeting to discuss the capital controls issue.

¶6. (SBU) Following is the text of the DAS Dohner letter delivered to Mr. Hung.

BEGIN TEXT

Thank you for the opportunity to consult on the economic challenges you are facing as a result of your rising stock market and strong capital inflows. I have been working on Asian economic issues for many years, and have come to admire the economic dynamism, commitment to strong policies, and solid growth in the region, including in Vietnam. I accompanied Secretary Paulson on his visit to Hanoi for the APEC Ministers meeting and had the pleasure of meeting with Deputy Finance Minister Ha and other members of Vietnam's economic team. Vietnam's accession to the WTO is a highlight of the progress that Vietnam is making by opening up to the world economy.

Currently, Vietnam is facing a specific challenge in dealing with capital inflows that have contributed to a rapid rise in the stock market. We have heard that your government is considering various policy options, including the imposition of capital controls on foreign portfolio investments, such as a one-year lock-up period. As an economic partner with Vietnam, we wanted to consult so that we fully understand your issues and see if we can be of assistance.

The U.S. Government has encouraged open capital markets, since the ability to transfer capital freely into and out of a country is important to promoting foreign investment, to the development of

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domestic capital markets, and to encouraging strong and sustained growth.

Based on the experience of other countries with capital controls, we believe that controls have negative repercussions on an economy, on balance. The imposition of controls undermines investor confidence, and generally have costs that are often unanticipated at the time the controls are introduced. Additionally, capital controls require significant administrative costs, and investors typically find ways around the controls over time. As a result, the effectiveness of controls tends to decline over time while their costs increase.

There may be other policy alternatives available to you that would help achieve your objectives at a lower economic cost, such as setting limits on margin loans and unsecured loans for equity investments, faster liberalization of capital outflows, equitization of state-owned enterprises (to provide greater supply of equity market instruments to meet demand), and greater exchange rate flexibility.

Also, I'd like to provide you an update on our technical assistance partnership. As you may know, the Treasury Department in recent months has stepped up our technical engagement with the Finance Ministry. In particular, Treasury will be sending a technical assistance team to Hanoi in March to move forward on the Tax Administration Technical Assistance our governments have been discussing. This team will seek to draft a Terms of Reference and develop a detailed work plan for 2007 in the areas of human resources, management training and internal investigations. Further, more Treasury teams will visit over the next several months to start developing technical assistance projects in the areas of financial sector and capital market development. We value this engagement and look forward to continued consultations.

If you wish I would be happy to continue discussions on capital controls and their alternatives via a phone call or an exchange of letters if you wish.

END TEXT

¶7. (SBU) We will report any response that Mr. Hung has to the letter. The government largely shuts down beginning on February 16 for the Tet holiday and does not fully resume business until February 26.

Unconfirmed report not to adopt controls

¶8. (SBU) There was a market report today from J.P. Morgan that the National Monetary and Finance Committee of the Vietnam Government met on February 13 and voted against SBV proposal to introduce financial controls. We were not able to confirm the facts of this report. A contact at the State Security Commission (SSC) told us this committee did meet on February 12 to discuss the recent developments in the securities market but he could not confirm any information on any vote. His opinion was that the Prime Minister would not sign the SBV's proposal because of awareness of the negative experience in Thailand after its government introduced controls.

¶9. (SBU) Mr. Hung at OOG was also not aware of this meeting. He commented that the GVN wants to develop the securities market and would not plan to introduce non-market control measures to reduce market activities. At the same time, he also noted that because the securities market is still young and growing hot recently, it would need close monitoring and good management. He underscored that any measures taken would be considered carefully to ensure that they comply with WTO commitments.

¶10. (SBU) Another contact at the Ministry of Finance could not confirm the reported February 13 meeting. He predicted that the securities market would continue to grow and he argued it is not likely that the GVN would introduce control measures that would have negative impacts on the market.

Comment

¶11. (SBU) COMMENT: We should know by the end of the week whether Vietnam launches a Tet offensive against capital inflows or if cooler heads prevail in deciding how to deal with a hot stock

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market.

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